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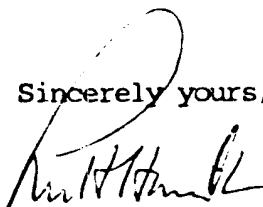
Honorable William J. Casey
Director of Central Intelligence
Washington, D.C. 20505

Dear Mr. Casey:

The bill H.R. 3963, "Defense Intelligence Commercial Entities Act," introduced by Congressman G. William Whitehurst, has been referred to this Committee. The Committee would appreciate receiving your views on H.R. 3963.

With best wishes, I am

Sincerely yours,


Lee H. Hamilton
Chairman

Enclosures: H.R. 3963
Section-by-Section Analysis

TITLE V - SUPPORT FOR DEFENSE INTELLIGENCE
COLLECTION ACTIVITIES

SEC. 501. (a) Subtitle A of Title 10, United States Code, is amended by adding the following new chapter after Chapter 18:

"CHAPTER 19 - SUPPORT FOR INTELLIGENCE

SEC.

- 391. Purpose of this chapter.
- 392. Definition.
- 393. Authority to conduct commercial cover.
- 394. Authority to acquire logistic support, supplies, and services.
- 395. Oversight.
- 396. General Provisions.

"SEC. 391. Purpose of this chapter.

The purpose of this chapter is to provide statutory authority for the Secretary of Defense or the Secretaries of the Military Departments to conduct support activities necessary for authorized and appropriately coordinated intelligence collection activities of the Department of Defense.

"SEC. 392. Definition.

a. "Intelligence collection activities" means the collection of foreign intelligence or counterintelligence information by intelligence components of the Department of Defense.

b. "Intelligence support activities" means those activities described in sections 393 and 394, below.

c. "Commercial cover" means a business entity that is established solely to conceal the role of an intelligence component of the Department of Defense as it performs intelligence collection activities.

"SEC. 393. Authority to conduct commercial cover.

a. "The Secretary of Defense or the Secretaries of the Military Departments, after consultation with the Director of Central Intelligence and the Director of the Federal Bureau of Investigation, as appropriate, may establish and conduct commercial entities such as corporations, partnerships, sole proprietaries, and other business entities as commercial covers to support intelligence collection activities of the Department of Defense, as defined herein. Such commercial entities may be established only upon written certification by the Secretary concerned that commercial cover is necessary to the conduct of authorized intelligence collection activities.

b. "The establishment and operation of commercial entities pursuant to this section shall be in accordance with prevailing commercial practices so long as such practices are not inconsistent with the purposes of commercial cover. To this end, laws applicable to federal appropriations, federal property management, federal acquisitions, federal employment and government corporations shall not apply to the establishment and operation of commercial covers upon the written certification by the Secretary concerned or his designee for the purpose that the application of such laws would risk the compromise of commercial cover.

c. "The Secretary of Defense or the Secretaries of the Military Departments, or their designees, are authorized to deposit and withdraw funds appropriated for the Department of Defense used to conduct commercial cover and funds generated by the business entities authorized by this section in banks or other financial institutions.

d. "Funds generated by such business entities may be used to offset necessary and reasonable expenses incurred by the commercial cover. As soon as practicable, funds generated by a commercial cover that are no longer necessary for the conduct of that commercial cover shall be deposited in the Treasury of the United States as miscellaneous receipts.

e. "Upon the liquidation, dissolution, sale, or other final disposition of a commercial cover established and conducted under the provisions of this section, the funds, after obligations are met, shall be deposited in the Treasury of the United States as miscellaneous receipts.

"SEC. 394. Authority to acquire logistic support, supplies, and services.

a. "The Secretary of Defense or the Secretaries of the Military Departments, or their designees, may acquire any goods, services, property, buildings, facilities, space, insurance, licenses and any equipment necessary in order to establish or maintain a commercial cover.

b. "Acquisitions made under the provisions of this section are to be made utilizing procedures consistent with prevailing commercial practice so long as such practices are not inconsistent with the purposes of the commercial cover. To this end, laws applicable to federal acquisitions, federal appropriations, federal property management, and federal employment shall not apply where the application of such laws would risk compromise of the commercial cover.

"SEC. 395. General Provisions.

a. "The Secretary of Defense shall promulgate regulations to ensure oversight, operational effectiveness, and accountability of the intelligence support activities conducted pursuant to sections 393 and 394 of this title.

b. "The Secretary of Defense or Secretaries of the Military Departments shall ensure that elements of the Department of Defense that undertake intelligence support activities pursuant to this chapter conduct an annual review and audit of such support activities.

c. "Intelligence support activities authorized under this chapter shall be protected pursuant to 50 U.S.C. 403(d)(3).

(b) The table of chapters at the beginning of subtitle A of such title and at the beginning of Part I of such subtitle are each amended by inserting after the item relating to chapter 18 the following new item:

"19. Support for Intelligence.....391".

TITLE V

SUPPORT FOR DEFENSE INTELLIGENCE COLLECTION ACTIVITIES

Section 501 adds a new chapter 19 to subtitle A of Title 10, United States Code, authorizing the establishment and conduct of corporations or other business entities to provide support for Department of Defense undercover intelligence collection activities.

Proposed subsection 391 states that the purpose of proposed chapter 19 is to provide the SECDEF and the Secretaries of the Military Departments to establish the statutory authority commercial covers to support intelligence collection activities.

Proposed subsection 392a defines a new term "intelligence collection activities". The use of a new term rather than the redefining of the term "intelligence activities" precludes the development of two definitions (E.C. 12333 & statutory) for the same term.

Proposed subsection 392b defines the term "intelligence support activities" to mean the establishment, acquisition and conduct of commercial cover systems and the acquisition of logistical support thereto as described in subsections 393 and 394.

Proposed subsection 392c defines a new term, "commercial cover", which is used throughout the proposed Chapter 19 of this title.

Proposed subsection 393a authorizes the Secretary of Defense or the Secretaries of the Military Departments to establish and conduct commercial covers as commercial entities. In making specific reference to consultation with the Director of Central Intelligence and the Director of the

Federal Bureau of Investigation, this subsection is not intended in any way to alter or derogate from the responsibilities and authority of the Chief of Mission to a foreign country under 22 U.S.C. 3927 for direction, coordination, and supervision of all U.S. Government employees in that country (except for employees under the command of a U.S. area military commander) or from established procedures for coordination with the Secretary of State in the conduct of clandestine activities. Subsection 393a further states that the establishment of a commercial cover requires a finding in the form of a written certification by the Secretary responsible for the commercial entity that the commercial cover is necessary to the conduct of authorized intelligence collection activities.

Proposed subsection 393b requires that the establishment and operation of such commercial covers be in accordance with prevailing commercial practice. Federal statutes that regulate the establishment and operation of commercial and industrial type government activities shall not apply to the establishment and operation of commercial covers conducted pursuant to this section when there is a written certification by the Secretary concerned or his designee that compliance with such statutes would risk compromise of the commercial cover. It is not intended that the authorities contained in this section will relieve the Department of Defense from any requirements of applicable laws. Any exemptions apply only to the operations of the commercial cover. Commercial covers must of necessity conform to standard commercial practices. Compliance with statutory requirements that govern routine government procurement and financial transactions would not conform with such prevailing commercial practices and would flag a commercial cover entity as being connected with the United States Government, thus risking the security of the commercial cover and the underlying intelligence collection activities. In the past, Congress has exempted the FPI from certain procurement and financial requirements, e.g., the Anti-Deficiency Act, 31 U.S.C. 1341, and the Department of Defense is proposing that similar exemptions be authorized for intelligence support activities. It is virtually impossible to foresee and list by citation every statutory requirement that may be incompatible with intelligence support activities. Therefore, subsection 393b describes the exemptions categorically in order to capture and embody all the provisions that would risk compromising the commercial cover. Such statutes encompass laws applicable to federal appropriations, federal property management, federal acquisitions, federal employment, and government corporations. These categories of law are defined below.

"Federal acquisitions" means acquiring real estate, goods or services for the United States Government. These activities are principally governed by Titles 41 and 10 of the United States Code. Title 41 requirements that may be incompatible with intelligence support activities include:

41 U.S.C. 5 which establishes the requirement to advertise proposed purchases and proposed contracts for supplies or services.

41 U.S.C. 35 which requires the inclusion of contract provisions such as the Walsh-Healey Act representations and stipulations.

41 U.S.C. 46 and 48c which establish the requirement to purchase blind-made products.

41 U.S.C. 255 which limits advance payments to contractors.

41 U.S.C. 253 which requires full and open competition.

Title 10 requirements that may be incompatible with intelligence support activities include:

10 U.S.C. 2207 which prohibits contracting unless the contract contains specific provisions.

10 U.S.C. 2276 which makes the contractor's books subject to Government audit.

10 U.S.C. 2301 which prohibits cost-plus-a-percentage-of-cost contracts. This section also subjects a commercial cover to small business set-asides. This may conflict with prevailing commercial practice.

10 U.S.C. 2304 which limits the use of negotiated procurements. Formal advertisement (sealed bids) may not be consistent with prevailing commercial practice.

10 U.S.C. 2306 which places restrictions on the kinds of contracting that may be used. These restrictions may conflict with prevailing commercial practice. This section also creates a right to examine all books, records, etc. of the contractor or subcontractor. This may also identify the intelligence support activity as a U.S. Government entity.

10 U.S.C. 2307 which prohibits certain advance payments for property and services. This may conflict with prevailing commercial practice.

10 U.S.C. 2313 which creates a right to inspect plants and audit books of certain contractors and subcontractors. Such an inspection would identify the contracting agency as a United States Government entity.

10 U.S.C. 2360 which creates a right for students contracting with the Government to be entitled to be considered as employees which may identify the contracting agency as a United States Government entity.

10 U.S.C. 2381 which requires certain measures for non-negotiated procurements which will identify the contracting agency as a United States Government entity (surety bonds, charges, etc.).

10 U.S.C. 2384 which requires supplies furnished to a military department to be uniquely marked, which will identify the contracting agency as a United States Government entity.

10 U.S.C. 2631 which restricts transportation of supplies to U.S. Flag Vessels. This may conflict with prevailing commercial practice.

"Federal property management" means the control and use of federal real and personal property. These activities are principally governed by Titles 40 and 10 of the United States Code. Restrictions that may be incompatible with commercial covers include:

40 U.S.C. 34 which limits the leasing of space in the District of Columbia.

40 U.S.C. 33a which establishes restrictions on construction loans for office buildings by Government corporations.

40 U.S.C. 129 which establishes limits on a Government corporation's leasing of buildings in addition to the limitation on rental rates and prohibits the inclusion, in any lease, of any provision regarding the repair of real property.

10 U.S.C. 2662 which requires reporting of certain real estate transactions to Congress 30 days in advance of the transaction.

10 U.S.C. 2672 restricts agency authority to acquire an interest in land to \$100,000 or less.

10 U.S.C. 2676 limits authority to acquire land unless acquisition is expressly authorized by law.

"Federal employment" means restrictions, rights, duties, and entitlements flowing from Part III of Title 5 of the United States Code. The intent of this section is to exclude from the application of Title 5, United States Code, employees of the commercial cover who are not federal employees occupying positions within the commercial cover. The restrictions, rights, duties, and entitlements that may be incompatible with prevailing commercial practices include:

5 U.S.C. 3101 et seq. which limits the authority to appoint employees.

5 U.S.C. 5101 et seq. which establishes classes of employees and prescribes levels of pay for those classes.

5 U.S.C. 4101 et seq. which establishes training programs.

5 U.S.C. 4301 et seq. which establishes a performance rating system for employees, including minimum due process.

5 U.S.C. 6101 et seq. which establishes a leave and attendance system.

5 U.S.C. 7101 et seq. which establishes a system for adverse actions, including removal.

5 U.S.C. 8101 et seq. which provides for insurance and other entitlements.

"Government Corporations" means a corporation that is owned by the Federal Government. While commercial covers are not Government corporations in the classical sense, they nonetheless meet definitions set out in 31 U.S.C. 9101(1). Government corporations are principally governed by Title 31 of the United States Code. Requirements that pertain to Government corporations that may be incompatible with commercial covers include:

31 U.S.C. 9102 which requires that each corporation established or acquired by an agency be specifically authorized by Congress.

31 U.S.C. 9103 which requires an annual budget submission to Congress.

31 U.S.C. 9107 which requires Comptroller General's approval prior to the consolidation of a corporation's cash.

31 U.S.C. 9108 which limits the obligations that may be issued by a Government corporation.

It is intended that commercial covers utilize these exemptions only to the extent that it is necessary, and that they be conducted in a manner that is generally consistent with ordinary commercial practice. Adequate safeguards are provided in the legislation and the Department's own procedures will further ensure the proper application of the exemptions and the appropriate use of funds.

Subsection 393c authorizes the deposit and withdrawal of appropriated and generated funds in banks and other financial institutions.

Subsection 393d requires that all proceeds generated by a commercial cover that are no longer necessary to offset necessary and reasonable expenses of the commercial cover, revert to the U.S. Treasury as miscellaneous receipts.

Subsection 393e requires that funds resulting from a final disposition of a commercial cover, after all obligations have been met, shall be deposited in the United States Treasury as miscellaneous receipts.

Proposed subsection 394a grants to the Secretary of Defense or the Secretaries of the Military Departments, or their designees, the authority to acquire necessary services, personalty, fixtures, and realty in order to support a commercial cover.

Proposed subsection 394b requires that acquisitions made pursuant to subsection 394a utilize procedures that are consistent with prevailing commercial practice. The subsection further provides that such acquisitions shall be exempt from laws governing federal acquisitions, federal appropriations, federal property management, and federal employment where the application of such laws would risk the compromise of the commercial cover. It is not intended that the authorities contained in this section will relieve the Department of Defense from any requirements of applicable laws. Any exemptions apply only to the operations of the commercial cover. For a discussion of these laws see the analysis above pertaining to proposed subsection 393b.

Proposed section 395a requires the Secretary of Defense to promulgate regulations to ensure oversight, operational effectiveness, and accountability of all intelligence support activities undertaken pursuant to this chapter.

Proposed subsection 395b requires the Secretary of Defense, or the Secretaries of the Military Departments to ensure that an annual review and audit is conducted of each intelligence support activity.

Proposed subsection 395c makes it clear that all intelligence support activities undertaken pursuant to this chapter are to be protected from unauthorized disclosure as set forth in 50 U.S.C. 403(d)(3).